

BEFORE THE DEPARTMENT OF REVENUE
OF THE STATE OF MONTANA

In the matter of the amendment of) NOTICE OF PUBLIC HEARING ON
ARM 42.13.111, 42.13.802, 42.13.803,) PROPOSED AMENDMENT
42.13.804, 42.13.805, and 42.13.806)
regarding distilleries)

TO: All Concerned Persons

1. On January 13, 2014, at 10:30 a.m., the Department of Revenue will hold a public hearing in the Third Floor Reception Area Conference Room of the Sam W. Mitchell Building, located at 125 North Roberts, Helena, Montana, to consider the proposed amendment of the above-stated rules. The conference room is most readily accessed by entering through the east doors of the building.

2. The Department of Revenue will make reasonable accommodations for persons with disabilities who wish to participate in this public hearing or need an alternative accessible format of this notice. If you require an accommodation, please advise the department of the nature of the accommodation needed, no later than 5 p.m. on January 3, 2014. Please contact Laurie Logan, Department of Revenue, Director's Office, PO Box 7701, Helena, Montana 59604-7701; telephone 406.444.7905; fax 406.444.3696; or e-mail lalogan@mt.gov.

3. The rules proposed to be amended provide as follows, stricken matter interlined, new matter underlined:

42.13.111 DEFINITIONS The following definitions apply to this subchapter:

(1) and (2) remain the same.

(3) "Contract packaging" means blending, bottling, packing, and/or filling of a distilled spirits product by a domestic distilled spirits plant for another distilled spirits plant.

(3) remains the same but is renumbered (4).

(5) "Distilled at the microdistillery" means the process of vaporization and subsequent condensation of a beverage containing ethyl alcohol that occurs at the licensed premises.

(6) "Distilled spirits" means alcoholic beverages that contain ethyl alcohol and generally are the result of distillation of fermented materials. Examples include whiskey, gin, vodka, cordials, liqueurs, and flavored brandies. Distilled spirits do not include alcoholic beverages that are defined as beer or wine by the Montana Alcoholic Beverage Code.

(7) "Distilled spirits plant" means a plant at which distilled spirits are manufactured, produced, aged, stored, packaged, or bottled.

(4) remains the same, but is renumbered (8).

(9) "Microdistillery" means a distillery located in Montana that produces 25,000 gallons or less of liquor annually.

(5) remains the same, but is renumbered (10).

~~(6)~~(11) "Patio/deck" means a specific area designated on a floor plan which shall be completely enclosed by at least a 3-foot fence or wall, immediately adjacent to and accessible from inside the licensed premises an outdoor area that is part of the licensed premises, specifically designated on a floor plan, with a perimeter barrier and immediately adjacent to, and accessible from, the indoor portion of the licensed premises.

(12) "Perimeter barrier" means a barrier enclosing the perimeter of the patio/deck portion of a licensed premises, which defines the boundary of the licensed premises in a way that:

(a) clearly marks for patrons, licensees, licensees' employees, investigators, local law enforcement, and the general public where consumption of alcohol is allowed;

(b) impedes access to the service areas by underage persons or others who may attempt to enter the premises without the licensee's knowledge; and

(c) consists of a fence or wall at least three feet high, or an alternative barrier that accomplishes the same purposes and is approved by the department. A perimeter barrier may be with or without entrances from the parking lot, sidewalk, or other areas beyond the patio/deck regardless of whether those areas beyond the licensed premises are land or water. In the case of a patio/deck which abuts a river, lake, or other body of water, the edge of the water may serve as a portion of the perimeter barrier, subject to department approval.

(7) and (8) remain the same, but are renumbered (13) and (14).

~~(9)~~(15) "Premises" means one building or a specific portion or portions of one building as described on the floor plan, identified by a unique address and approved by the department. The premises shall contain all service areas used by the licensee and the licensee's patrons and those service areas in which the licensee operates outside of and attached to the licensed building and to which patrons are permitted free access from the building. Premises includes a patio/deck.

(10) through (14) remain the same, but are renumbered (16) through (20).

AUTH: 16-1-303, 16-1-424, 16-9-1009, MCA

IMP: 16-1-424, 16-3-302, 16-3-311, 16-4-312, 16-4-404, 16-4-406, 16-4-1001, 16-4-1002, 16-4-1003, 16-4-1004, 16-4-1005, 16-4-1006, 16-4-1007, 16-4-1008, 16-6-104, MCA

REASONABLE NECESSITY: The department is proposing to amend ARM 42.13.111 to include new definitions and amend some existing definitions. New definitions are necessary to provide further clarification for terms that are used in subsequent rules in chapter 13. The additional definitions will better inform the industry and the public regarding the subject matter.

The definition of "patio/deck" is proposed to be amended to more closely mirror the definition in ARM 42.12.106. Creating continuity between the two rules will reduce confusion.

42.13.802 DOMESTIC DISTILLERIES (1) ~~Every distillery must report to the department, on a form prescribed by the department, the following information:~~

~~(a) the cost of the product per case price FOB Helena, Montana that the~~

distillery intends to sell to the department;

~~(b) the quantities of liquor shipped to the department; and~~

~~(c) the total number of proof gallons manufactured, distilled, rectified, bottled, or processed and sold nationwide. The department may issue a domestic distillery license to a person holding a federal basic permit for a distilled spirits plant.~~

~~(2) The department will generate a posted price from the distillery's case cost. The posted price shall include excise and license taxes as provided in Title 16, part 4, MCA, rounded to the nearest nickel increment. The department shall advise the distillery of the per bottle tax amount. All domestic distilleries must meet the premises suitability requirements in ARM 42.12.122 and 42.12.139. A domestic distillery's premises may include more than one building if the land on which the buildings are located is contiguous and the licensee has complete control over and possessory interest in the property.~~

~~(3) The distillery shall collect the tax for any retail sale made directly to the consumer. A domestic distillery licensee shall maintain records documenting its business operations including, but not limited to, the production, storage, and processing of liquor on the premises.~~

~~(4) The posted price will remain the price until a revised form is submitted and approved by the department. A revised quote for regular listed products shall be submitted not less than 60 days prior to the effective date of the department's quarterly price book. A domestic distillery may qualify as a microdistillery to sell liquor it produces at the microdistillery's sample room for on- or off-premises consumption if it distills 25,000 gallons or less of liquor annually at the microdistillery and meets the requirements in ARM 42.13.805.~~

AUTH: 16-1-303, 16-1-424, MCA

IMP: 16-1-404, 16-4-311, 16-4-312, 16-4-501, MCA

REASONABLE NECESSITY: The department is proposing to amend ARM 42.13.802 to better inform the industry about the requirements for obtaining a domestic distillery license.

The language proposed to be stricken from (1) through (4) will be relocated within ARM 42.13.803, 42.13.804, and 42.13.805, as appropriate. The proposed amendments will place related content together within these rules to better inform the industry.

The proposed new language in (1) clarifies to whom the department may issue a domestic distillery license. This will better inform the industry and public that certain federal permitting is required.

The proposed new language in (2) cites the specific suitability requirements that must be met in order to be considered for licensure. The department further proposes to amend this rule to allow for the manufacturing premises to include more than one building provided it meets certain requirements. Storage of product, whether for aging purposes or preparation of shipment, requires space which is not always available at the distillery. Allowing for additional buildings to be included on the premises, provided they are contiguous and the licensee has complete control over and possessory interest in the property, will mirror federal laws related to distilled spirit plants.

The proposed new language in (3) better informs the industry that certain documents must be maintained. Documentation is needed to ensure the licensee is compliant with state laws and rules.

The proposed new language in (4) is intended to enhance the licensee's understanding on the requirements that must be met in order to qualify as a microdistillery. These proposed amendments are intended to help educate the industry and ensure they stay compliant with state laws.

The department further proposes to add the term "domestic" to the title to clarify that the rule applies only to distilleries located in Montana. The proposed amendment to the title is intended to enhance understanding and reduce confusion.

42.13.803 DOMESTIC DISTILLERIES - PRODUCT PRICING (1) The department will provide each distillery with a standard quotation and specification form to report the necessary information for each product the distillery desires to sell in Montana.

(2) remains the same.

(3) The distillery will provide the department with the total number of proof gallons manufactured, distilled, rectified, bottled, or processed, and sold nationwide to determine the distillery's tax and mark-up brackets.

~~(3)~~(4) The department will:

(a) generate the posted price per bottle from the distillery's case cost; and. The posted price includes the distillery's case cost delivered to Helena, Montana, the department's current freight rate to agency liquor stores, the state's mark-up, liquor excise tax and liquor license tax, rounded to the nearest five-cent increment.

~~(b) notify the distillery of the posted price per bottle.~~

~~(4) The distillery may not sell the product below the posted price.~~

(5) and (6) remain the same.

~~(7) The department will notify the distillery of the liquor excise and liquor license tax per bottle.~~

AUTH: 16-1-303, 16-1-424, MCA

IMP: 16-1-404, 16-4-311, 16-4-312, 16-4-501, MCA

REASONABLE NECESSITY: The department is proposing to amend ARM 42.13.803 to enhance the industry's understanding with regard to the pricing of distilled spirits.

The proposed amendment to the title strikes the term "domestic" because (1) through (6) apply to all distilleries, not just domestic distilleries. The proposed amendment is intended to reduce confusion and increase understanding within the industry.

Section (1) is proposed to be amended to reflect that for tax purposes and to establish the product's posted price, a standard price quotation form is needed for each product intended to be sold in the state, including products that will only be sold at the distillery. The proposed amendments will help to ensure that the proper amounts are being reported and paid.

Section (3) is language the department is proposing to strike from ARM 42.13.802, and relocate into this rule, as the number of proof gallons the distillery

reports is a component of the pricing structure.

The department is proposing to amend (4) to include the elements that generate the posted price per bottle. The proposed amendments are intended to enhance understanding within the industry by adding more transparency into the pricing formula that is used.

The department further proposes to strike (4) and (7) from this rule and incorporate the language into ARM 42.13.804. As proposed to be amended, ARM 42.13.804 is the more appropriate location for the subject matter.

42.13.804 DOMESTIC MICRODISTILLERY - MONTHLY REPORTS TAX RETURN (1) Each ~~distillery~~ microdistillery shall electronically file with the department a monthly ~~tax report~~ Excise and License Tax Return, as required by 16-1-424, MCA, ~~showing reporting~~ the following information:

(a) the total number of ~~proof~~ gallons ~~manufactured, distilled, rectified, bottled, or processed and sold nationwide during the current calendar year~~ preceding calendar month to verify the distillery qualifies as a microdistillery based on its production level;

(b) the total amount of liquor ~~provided to consumers~~ number of bottles transferred to the sample room for on-premises consumption with or without charge at the distillery; and

(c) the total number of bottles sold to consumers at retail for off-premises consumption; and

(d) the total amount of liquor excise tax and liquor license tax due for the month being reported.

(2) All product ~~provided to a consumer by the microdistillery~~ must have a standard quotation and specification form on file with the department. If no form is provided to the department or, at the department's discretion, if the form provided is or appears to be incomplete or inaccurate, the department may determine the per-bottle liquor excise tax and liquor license tax that the distillery must pay. The liquor excise tax and liquor license tax will be determined by using the higher of:

(a) the retail selling price set by the microdistillery as the posted price; or

(b) an average cost for products within the same category and size by other domestic distilleries that sell product to the department.

(3) The department will notify the microdistillery of the posted price per bottle, the per-bottle liquor excise tax, and the liquor license tax amounts as determined in (2).

~~(2)~~(4) The ~~form~~ return must be accompanied by payment of the tax pursuant to 16-1-424, MCA, on or before the 15th day of each month for liquor sold during the previous month.

AUTH: 16-1-303, 16-1-424, MCA

IMP: 16-1-404, 16-1-424, 16-4-311, 16-4-312, 16-4-501, MCA

REASONABLE NECESSITY: The department proposes to amend ARM 42.13.804 to enhance the microdistillery licensee's understanding of their tax obligation for sales that occur at the distillery.

The proposed amendment to the title will change the reference from

"distilleries" to "microdistilleries" and replace the word "reports" with "tax return" to better reflect the content of the rule. A tax return is required for sales that occur at a microdistillery. Distilleries that do not meet the requirements to be a microdistillery are prohibited from selling product to anyone other than the department, whether for on- or off-premises consumption. Specifying "microdistilleries" in the title will reduce confusion as to who must submit a monthly tax return.

The department is proposing to amend (1) by referencing the name of the tax return to be filed. This will reduce any confusion that exists within the industry. An amendment is also being proposed to require the microdistillery to file the tax return electronically. The department developed a user-friendly, on-line tax return for microdistilleries to report and pay their taxes. Filing electronically is fast, convenient, and secure.

Section (1)(a) is proposed to be amended to create continuity with 16-4-310, MCA. In order to be a microdistillery, the distillery must distill less than 25,000 gallons of liquor annually. Requiring the distillery to report the amount of liquor distilled on the premises will ensure it meets the microdistillery requirement and will help ensure a level playing field amongst other licensed distilleries.

Section (1)(b) is proposed to be amended to designate how the microdistillery is required to report the amount of liquor provided for on-premises consumption within their sample room. This will reduce existing confusion within the industry.

Section (1)(d) is proposed to be added because reporting the tax is the responsibility of the microdistillery for sales that occur at the premises per 16-1-424, MCA.

The department is proposing to add new (2) to ensure microdistilleries calculate and pay the correct amount of tax for product sold. The amount of tax per bottle is derived from the case price filed with the department. If the microdistillery fails to submit a price filing or submits an unreasonable price filing, the proposed rules enable the department to generate an accurate tax amount based on either the retail selling price or pricing from similar Montana distilled products. This proposal will ensure all distilleries pay the correct amount of tax and will help eliminate the potential for any distilleries trying to circumvent their tax obligation.

Section (3) is language the department is proposing to strike from ARM 42.13.803 and relocate into this rule, as it directly correlates with the monthly tax return.

The department also proposes to add a missing implementing citation.

42.13.805 DOMESTIC DISTILLERY - SAMPLES MICRODISTILLERY
SAMPLE ROOMS (1) Product samples may only be provided in the A
microdistillery may have one sample room as shown on the floor plan which has
been submitted and approved by the department to provide consumers with samples
of liquor products that the microdistillery produced at its licensed premises.

(2) The sample room must be located on the licensed premises and cannot
be used for providing samples until approved by the department.

(3) All liquor products provided to a consumer for on- or off-premises
consumption in the sample room must have been produced at the microdistillery.
For a product to be considered as having been produced at the microdistillery, the
following criteria must be met:

(a) as measured by proof gallons on a monthly basis, at least 90 percent of the aggregate amount of liquor provided for on- and off-premises consumption in the sample room must have been distilled at the microdistillery; and

(b) all liquor transferred into the sample room for on- or off-premises consumption must contain alcohol that was distilled at the microdistillery.

(4) Any microdistillery that is licensed and has a department-approved sample room as of March 1, 2014, has until October 1, 2015, to come into compliance with (3)(a). Any such microdistillery that does not meet (3)(a) shall, at a minimum, maintain the percentage it has as of March 1, 2014, until October 1, 2015.

(5) Prior to providing any liquor product to consumers in its sample room, a microdistillery shall notify the department of the percentage of alcohol in each proof gallon of the product that is distilled at the microdistillery. The microdistillery shall also notify the department of any changes to these percentages prior to providing the changed product to consumers. For example, if half the alcohol in a product (as measured by proof gallons) was distilled at the microdistillery, while the other half was produced elsewhere, the microdistillery would report that the product contains liquor that is 50 percent distilled at the microdistillery.

(2)(6) A domestic distillery microdistillery is not a retail licensee as defined in 16-4-201, MCA.

(3)(7) A sample room may include a deck or patio patio/deck, as long as the deck or patio is immediately adjacent to the distillery sample room and can only be accessed from the distillery. The deck or patio must be enclosed in such a manner as to restrict its access and view from the general public on the street or sidewalk if it has the required perimeter barrier, as defined in ARM 42.13.111, and is in compliance with fire safety regulations.

AUTH: 16-1-303, MCA

IMP: 16-4-310, 16-4-312, MCA

REASONABLE NECESSITY: The department is proposing to amend ARM 42.13.805 to add clarification with regard to microdistillery sample rooms.

The proposed amendment to the title will better reflect the content of the rule as amended. Sample rooms are only allowed if the distillery meets the requirements to be a microdistillery. Amending the title will reduce confusion as to which type of distillery is permitted to have a sample room. The proposed amendments to renumbered (6) will make reference to microdistilleries rather than domestic distilleries as well.

Section (1) is proposed to be amended to add clarity and enhance understanding within the industry that only one sample room is permissible per microdistillery, and that liquor samples offered at the sample room must have been produced on the premises pursuant to 16-4-310, MCA. The stricken language in (1) pertaining to sample room approval by the department has been moved to (2).

New (2) is being proposed to inform the industry that sample rooms must be located on the premises of the microdistillery and that use of the sample room cannot commence until approved by the department. This will help ensure industry compliance.

New (3) is being proposed to inform the industry as to the types of liquor

products that are allowed to be sold in a microdistillery's sample room because administrative ambiguity exists in the use of imported bulk spirits by microdistilleries and necessitates administrative rules. The added clarification is intended to ensure that all microdistilleries located in Montana operate under the same regulations while still maintaining the intent of the 2005 Legislature. Proposed new (4) provides additional detail for complying with (3), and new (5) provides the necessary reporting requirements.

Section (7) is proposed to be amended to be consistent throughout the industry relative to the requirements for a "patio/deck." The proposed amendment is intended to mirror ARM 42.12.106, which defines "patio/deck" for on-premises retail establishments, to create consistency within the rules and to reduce any confusion within the industry or the general public.

The department further proposes to update the implementing citations to include the statute that describes the term "produces."

42.13.806 USE OF OUTSOURCED ALCOHOL DISTILLED SPIRITS IN THE MANUFACTURING OF DISTILLED SPIRITS (1) A distillery ~~or microdistillery~~ licensed by the department and located in Montana may import bulk distilled spirits that uses alcohol from another distilled spirits plant ~~in order to distill, rectify, blend, or manufacture its own alcoholic beverages is required to request by requesting~~ such products through the department on a form supplied by the department. The distillery may only use the acquired distilled spirits:

(a) to distill, rectify, blend, or manufacture its own distilled spirits; or

(b) for contract packaging purposes.

(2) A distillery ~~or microdistillery~~ may only obtain alcohol distilled spirits from sources authorized by the federal government, such as an entity that holds a basic permit or industrial permit.

(3) The department will process the request and notify the distilled spirits plant, specified by the distillery ~~or microdistillery~~, of the quantities, proof, types, and sizes of alcohol distilled spirits to be delivered to the distillery ~~or microdistillery~~.

(4) ~~The distillery or microdistillery may not bottle and sell alcohol acquired from the distilled spirits plant without using it in their own distilling, rectifying, blending, or manufacturing process first.~~

(5) The distillery ~~or microdistillery~~ must keep all alcohol distilled spirits acquired from a another distilled spirits plant ~~on the licensed premises at the distillery and the distilled spirits may not resell, transfer, or give away the alcohol.~~ A distillery ~~or microdistillery~~ must receive preapproval from the department to destroy or otherwise dispose of any alcohol distilled spirits the distillery ~~or microdistillery~~ acquired from another distilled spirits plant.

~~(6)~~(5) A distillery ~~or microdistillery~~ must document and maintain records at their its place of business of for all alcohol distilled spirits acquired from a another distilled spirits plant and document how it was used. The department may make an examination of any such distillery ~~or microdistillery's~~ records as it pertains to this section at any time.

AUTH: 16-1-303, MCA

IMP: 16-1-401, 16-1-404, 16-3-214, MCA

REASONABLE NECESSITY: The department is proposing to amend ARM 42.13.806 to provide clarification on the use of outsourced distilled spirits obtained from another distilled spirits plant.

The proposed amendment to the title will reduce confusion by appropriately referencing distilled spirits rather than the more broad term of alcohol. The statute allows for the importation of bulk distilled spirits; however, other forms of alcohol are not permissible under 16-1-401, and 16-1-404, MCA.

Throughout the rule, references to microdistilleries are proposed to be stricken. The department proposes these amendments as the use of outsourced distilled spirits applies to all distilleries. However, microdistilleries are permitted to sell in their sample room only products that were distilled on their premises and meet the requirements of ARM 42.13.805.

Section (1) is proposed to be further amended to allow for contract packaging and is defined in ARM 42.13.111. Contract packaging is permissible by federal law. Amending the rule to allow contract bottling creates consistency with federal and state law.

Sections (4) and (5) are proposed to be blended together to enhance readability and understanding, and (6) is proposed to be renumbered and amended to require distilleries to maintain records on how they used the acquired outsourced distilled spirits. Maintaining records will ensure distillery compliance relative to how the final product can be sold and to whom.

4. Concerned persons may submit their data, views, or arguments, either orally or in writing, at the hearing. Written data, views, or arguments may also be submitted to: Laurie Logan, Department of Revenue, Director's Office, PO Box 7701, Helena, Montana 59604-7701; telephone 406.444.7905; fax 406.444.3696; or e-mail lalogan@mt.gov and must be received no later than January 20, 2014.

5. Laurie Logan, Department of Revenue, Director's Office, has been designated to preside over and conduct the hearing.

6. An electronic copy of this notice is available on the department's web site at www.revenue.mt.gov. It can be found by selecting the "Administrative Rules" link in the left hand column of the homepage under the "Public Meetings" heading. The department strives to make the electronic copy of this notice conform to the official version of the notice, as printed in the Montana Administrative Register, but advises all concerned persons that in the event of a discrepancy between the official printed text of the notice and the electronic version of the notice, only the official printed text will be considered. While the department also strives to keep its web site accessible at all times, in some instances it may be temporarily unavailable due to system maintenance or technical problems.

7. The Department of Revenue maintains a list of interested persons who wish to receive notices of rulemaking actions proposed by this agency. Persons who wish to have their name added to the list shall make a written request, which includes the name and e-mail or mailing address of the person to receive notices

and specifies that the person wishes to receive notice regarding particular subject matter or matters. Notices will be sent by e-mail unless a mailing preference is noted in the request. A written request may be mailed or delivered to the person in number 4 above or faxed to the office at 406.444.3696, or may be made by completing a request form at any rules hearing held by the Department of Revenue.

8. The bill sponsor contact requirements of 2-4-302, MCA, apply and have been fulfilled. The primary sponsor of HB 517, L. 2005, Representative Brady Wiseman, was notified by regular mail on August 8, 2013, and subsequently notified by regular mail on November 20, 2013.

9. The department complied with the requirements of 2-4-111, MCA, and determined that the proposed amendments to the rules contained in this notice will not significantly and directly impact small businesses. There are fewer than 15 microdistilleries in Montana, and most are already in compliance with the rules as proposed to be amended.

/s/ Laurie Logan
LAURIE LOGAN
Rule Reviewer

/s/ Mike Kadas
MIKE KADAS
Director of Revenue

Certified to Secretary of State December 2, 2013